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Via email only: pubcom@finra.org

RE: Regulatory Notice 17-20: Retrospective Rule Review on the Effectiveness and Efficiency of FINRA's Rules on Outside Business Activities and Private Securities Transactions

Integrated Management Solutions USA LLC ("IMS") is pleased to comment on Regulatory Notice ("RN") 17-20, a Retrospective Rule Review initiated by FINRA on the Effectiveness and Efficiency of its Rules on Outside Business Activities and Private Securities Transactions (the "Rule Review"). IMS is one of the largest providers of compliance consulting and financial accounting services to the financial services industry, including to about 100 FINRA members, among others types of financial services firms.[1] We counsel clients daily on the scope of required broker-dealer compliance activities under various FINRA, SEC and other rules and are often asked to assist clients when their self-regulatory organization ("SRO") examines the firm. Thus, we are constantly advising clients on how to comply with FINRA Rule 3270, "Outside Business Activities of Registered Persons"[2] ("OBA") and FINRA Rule 3280, "Private Securities Transactions of an Associated Person"[3] ("PST"). This includes what to do

[1] The statements in this comment letter incorporate the views of IMS, not those of our clients.

[2] "Registered Person" is defined as "…any person registered with FINRA as a representative, principal, or assistant representative pursuant to the NASD Rule 1000 Series, the FINRA Rule 1200 Series, or Municipal Securities Rulemaking Board (MSRB) Rule G-3." FINRA Rule 3170(a)(1), "Tape Recording of Registered Persons by Certain Firms."

[3] The Securities and Exchange Act (the "34 Act") defines "associated person" in 2 sections:
The term ''person associated with a broker or dealer'' or ''associated person of a broker or dealer'' means any partner, officer, director, or branch manager of such broker or dealer (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling, controlled by, or under common control with such broker or dealer, or any employee of such broker or dealer, except that any person associated with a broker or dealer whose functions are solely clerical or ministerial shall not be included in the meaning of such term for purposes of section 15(b) of this title (other than paragraph (6) thereof). 34 Act, Sec. 3(a)(18).

* * * * *

The term ''persons associated with a member'' or ''associated person of a member'' when used with respect to a member of a national securities exchange or registered securities association means any partner, officer, director, or branch manager of such member (or any person occupying a similar status or performing similar functions), any

when FINRA alleges that a Registered Representative at a firm and/or the firm itself has violated one or both of these Rules.

We laud FINRA for instituting periodic retrospective rule reviews, particularly for rules that have been in place for many years. We believe this creates an opportunity for FINRA to implement principle-based rule-making rather than merely promulgating and/or amending prescriptive rules. Both these rules call into question to what extent an employee, whether a Registered Person in FINRA Rule 3270 or an Associated Person in Rule 3280,[4] should keep his or her employer informed of his or her activities, both during business hours and at other times.

FINRA Rule 3270

FINRA Rule 3270 imposes a blanket prohibition (with two limited exceptions) on outside "business" activity that may generate compensation to a Registered Representative of a member firm unless such Representative first has notified his or her employer in writing about such activity. Specifically excluded are passive investments and activities governed by FINRA Rule 3280, i.e., PSTs. Once the Registered Representative provides the requisite notice to his or her employer, Supplementary Material .01 shifts the compliance burden to the employer to determine whether the proposed activity:

person directly or indirectly controlling, controlled by, or under common control with such member, or any employee of such member. 34 Act, Sec. 3(a)(21).

FINRA's definition largely tracks that of the SEC. "[P]erson associated with a member" or "associated person of a member" means: (1) a natural person who is registered or has applied for registration under the Rules of the Corporation; (2) a sole proprietor, partner, officer, director, or branch manager of a member, or other natural person occupying a similar status or performing similar functions, or a natural person engaged in the investment banking or securities business who is directly or indirectly controlling or controlled by a member, whether or not any such person is registered or exempt from registration with the Corporation under these By-Laws or the Rules of the Corporation; and (3) for purposes of Rule 8210, any other person listed in Schedule A of Form BD of a member; FINRA By-Laws, Article I, (rr).

A clearer definition is available in FINRA's Dispute Resolution Glossary: "**Associated Person** – An associated person is any person engaged in the investment banking or securities business who is directly or indirectly controlled by a FINRA member, whether or not they are registered or exempt from registration with FINRA. An associated person includes, but is not limited to, every sole proprietor, partner, officer, director, or branch manager of any FINRA member. This individual may also be referred to as a broker."

[4] Perhaps FINRA should consider harmonizing its definitions and using fewer of them, particularly when they essentially overlap.

(1) will interfere with or otherwise compromise the registered person's responsibilities to the member or its customers; or

(2) depending on "…the nature of the proposed activity and the manner in which it will be offered," confuse customers or the public as being part of the member's business; or

(3) is more properly subject to Rule 3280 on PSTs.

The member can then either restrict or prohibit the outside business activity. Regardless of the member's decision, for each such notice, it must maintain records in accordance with Rule 17a-4(e)(1) of the Securities and Exchange Act of 1934. In all events, burdensome and time-consuming compliance obligations are placed on the member firm.

From anecdotal reports, reports of FINRA disciplinary proceedings, experiences described by other commenters to this Rule Review and our own experience assisting clients charged with violations of this Rule, the OBA Rule is enforced vigorously by FINRA. This track record demonstrates that FINRA examiners are quite likely to fine the Registered Representative and/or the member for an OBA violation, resulting in a disciplinary record on the Registered Representative's Form U-4 or the firm's Form BD.

This history raises several issues. Is there a benefit to a firm's customers or the investing public, in general, from such a broad octopus of a definition of business activity, where even the merest possibility of compensation triggers the notice requirement? What risk-based principle is being implemented? Who benefits from knowing that someone sells a craft item he or she makes at a weekend crafts fair? Or that a Registered Representative rents out an apartment or half of a house? What about a Registered Representative who photographs weddings on the weekend? How is anyone deceived as to the nature of such activity? Does one have to give up all other interests and talents as the price of being a Registered Representative? True, these Registered Representatives may be earning compensation from this sampling of activities, but so what? Under no scenario are these securities-related activities.

In our view, the possibility of compensation is so amorphous a standard by which to judge the relevance of a Registered Representative's OBA as to be virtually useless. Compensation does not address the substance of the OBA, its impact on the firm and its customers, the investing public and even FINRA for determining whether someone's activities

violates a FINRA rule. Who is misled by the types of activities described above? What principle is being validated by the enforcement of FINRA Rule 3270?

Assuming the business activity is more consequential, it may raise significant supervisory questions. For example, suppose a registered person is either a Certified Public Accountant or an attorney or an insurance broker, earning both transaction-based compensation as a Registered Representative of a member firm, but also fees for professional services (perhaps, even performed for the member firm where he or she is registered)? How is a compliance person sufficiently knowledgeable to evaluate the activities of an attorney? There are many specialties in law and even if a compliance supervisor actively maintains his or her attorney's license, would he or she have the requisite knowledge to evaluate another attorney's specialized work? Moreover, since much of the work of an attorney is subject to a privilege of one kind or another, will that privilege be forfeited by the supervisory review by a non-lawyer or a lawyer who really is not intended to obtain such information and be protected?

Better Guidance on OBA

As currently written, there are no useful tests to determine whether an OBA should be reported other than the mere whiff of compensation. We note that the requirement for a Registered Representative is, initially, one of notice. Once that notice is given, the compliance people at the member firm must conduct an in-depth analysis of why the activity should be permitted, permitted with restrictions or simply prohibited. Then, a business record must be created and maintained by the member firm. We understand why FINRA likes those record-keeping requirements, but is there a benefit to the investing public, a firm and/or its customers? Better guidelines are needed, whether in the form of supplementary materials to Rule 3270 or FAQs. FINRA needs to articulate far more clearly the principles it is seeking to promote and accomplish in Rule 3270. Such guidelines should describe and explain why certain types of outside business activities warrant additional and continuous scrutiny and possibly jeopardize the investing public, a member firm, its customers and the reputation of FINRA as an effective regulator.

Enforcement Priorities

We have observed that when FINRA cites a Registered Representatives and/or a firm for a violation of FINRA Rule 3270, it almost always imposes a fine of at least several thousand dollars. We recommend that, as a policy, assuming Rule 3270 remains in effect (in one form or another), a Registered Representative's first violation of Rule 3270's notice requirement should only warrant a caution (unless there are other contributing factors and/or other rule violations).[5] Why damage someone's career in such a public way for failing to provide a notice for an activity that probably has no negative consequences for anyone, including FINRA's regulatory constituency? Is there really a benefit to the public to apprise them that someone has been acting as a landlord of residential property? That is simply cluttering up the Registered Representative's U-4 and may, if other violations have occurred, have the unintended effect of burying a significant rules violation in trivia.

Rule 3280

We believe this rule is significant, necessary and valuable to all of FINRA's constituencies: the member firms, their customers, the investing public and FINRA itself. Here, too, members would benefit from principle-based regulation. For example, the situation where dual-hatted individuals are both investment advisers and Registered Representatives (either at an affiliated firm or elsewhere). FINRA has long grappled to find a solution to the intrinsic conflicts of interest raised when an investment adviser rendering investment advice to a client also benefits from trade executions implementing that advice. We believe that more detailed FAQs would be helpful in this situation. We also note that supervisory responsibilities for dual-hatted individuals are placed on all the firms where such individuals are registered. Is such duplication truly productive and protective of a firm's customers, the firms involved and/or the investing public? This appears particularly problematic – and expensive – for an individual who has had no prior disciplinary issues.

[5] FINRA enforcement is not consistently applied. Some people sometimes wonder whether a FINRA examiner's salary and promotion prospects hinge on the number and amount of fines that person generates. That is a situation FINRA proscribes for determining the compensation of a research analyst; FINRA Rule 2241(b)(2)(F).

The Problem with Prescriptive Rules

Both of these rules have terms that attempt to capture every possible nuance of activity. While they seem to over-capture everything, they are impractical and fail miserably. Instead, the rules should simply establish a global principle that says that members are responsible for the activities of their associated persons to the extent that they might impact adversely on members or customers. It is sort of like that old standard that says that people should conduct themselves in accordance with fair and equitable principles of trade. We really don't need the details that the current rules provide. They are counter-productive and somewhat unnecessary.

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We appreciate the opportunity to comment on FINRA's Rule Review process and Rules 3270 and 3280 in particular. Should you have any further questions, please feel free to call Howard Spindel at 212-897-1688 or Cassondra Joseph at 212-897-1687, or contact us by e-mail at hspindel@integrated.solutions or cjoseph@integrated.solutions, respectively.

Very truly yours,

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